No. 92-312

In The

Supreme Court of the United States

October Term, 1992

JAMES E. CROZIER, CHAPTER 11 TRUSTEE,
Petitioner,

v.

THERON BRADFORD, TRUSTEE,
Respondent.

Petition For Writ of Certiorari To The Fifth Circuit Court of Appeals

RESPONDENT'S BRIEF IN OPPOSITION

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STATUTORY PROVISIONS

In addition to those statutes recited by Petitioner

11 USC § 1124(i)

Impairment of claims or interests. Except as provided in section 1123(a)(4) of this title, a class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan--

(1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interests;

11 USC § 1129(a)(9)(C)

Except to the extent that the holder of a particular claim has agreed to a different treatment of such claim, the plan provides that--

(C) with respect to a claim of a kind specified in section 507(a)(7) of this title, the holder of such claim will receive on account of such claim deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim.

11 USC § 1322(b)(2)

(b) Subject to subsections (a) and (c) of this section, the plan may--

(2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims;

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RESPONDENT'S BRIEF IN OPPOSITION

TO THE HONORABLE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The Respondent, Theron Bradford, respectfully requests that this Court deny the Petition for Writ of Certiorari submitted by the Petitioner, James E. Crozier.

SUMMARY OF ARGUMENT

Resolution of this appeal requires the reviewing court to discern Congressional intent with respect to the interest rate to be allowed under 11 USC § 506(b). The statutory language provides only that interest shall be allowed to oversecured creditors, without specifying an interest rate. The legislative history fails to address the issue also. The Fifth Circuit, therefore, turned to pre-Code practice to determine whether any substantial change is required based upon the language of § 506(b). The Fifth Circuit correctly held that under the Act, the majority of courts held that the contract rate of interest applied and that nothing in the Bankruptcy Code or its legislative history was intended to change that rule.

1. THE PETITION FAILS TO SATISFY SUPREME COURT RULE 10.1(C) AS THERE ARE NO SPECIAL AND IMPORTANT REASONS EVIDENT IN THIS CASE.

Petitioner seeks review of the opinion of the Fifth Circuit Court of Appeals pursuant to Supreme Court Rule 10.1(c), which provides:

1. A review on writ of certiorari is not a matter of right, but of judicial discretion. A petition for a writ of certiorari will be granted only when there are special and important reasons therefor. The following, while neither controlling nor fully measuring the Court's discretion, indicate the character of reasons that will be considered:

> When a state court or a United States court of appeals has decided an important question of federal law which has not been, but should be, settled by this Court, or has decided a federal question in a way that conflicts with applicable decisions of this Court.

Petitioner fails to establish that there are ". . .special and important reasons. . ." for review by this Court, or that this is ". . .an important question of federal law which has not been, but should be, settled by this Court. . . ." Petitioner does not contend that the opinion of the Fifth Circuit ". . .conflicts with applicable decisions of this Court."

Petitioner correctly cites the only Circuit Court of Appeals decisions which have considered this issue, Matter of Laymon, 958 F.2d 72 (5th Cir. 1992) reh. den. 964 F.2d 1145 and In re

Anderson, 883 F.2d 834 (9th Cir. 1987), both of which hold that the contract rate should apply under 11 U.S.C. § 506(b). No conflict exists among the circuits. Although Petitioner acknowledges this lack of conflict at the circuit level, it cites this Court to "a division among the lower Courts." Petition, p. 16. Divisions at the Bankruptcy Court level are insufficient to justify review by this Court. In addition, the "division" may not be as clear as Petitioner appears to believe, as the cases which he cites illustrate a clear trend. First, more cases have selected the contract rate than any other rate. At pages 16 and 17 of his Petition, he cites six cases holding the contract rate to be proper and two cases each holding the federal judgment rate, market rate, and legal rate to be proper. Second, more recent cases have tended to select the contract rate over other rates. The contract rate cases cited by Petitioner are dated 1992, 1987, 1989, 1986, 1986 and 1983. The market rate cases are dated 1987 and 1982. The legal rate cases are dated 1982 and 1981. The federal judgment rate cases, one of which is the opinion overruled by the Fifth Circuit in this case, are dated 1990 and 1992. (It is, perhaps, significant that the other case was written

by the same bankruptcy judge who wrote In re Laymon, 117 B.R. 856 (Bankr. W.D.Tex. 1980), and cites his opinion in Laymon as controlling.) Even this cursory review establishes the trend that the majority of recent cases have held that the contract rate of interest is the appropriate rate under 11 USC § 506(b).

Although Petitioner contends that this Court should review this case to interpret § 506(b) in light of its prior rulings in United States v. Ron Pair Enterprises, Inc., 109 S.Ct. 1026 (1989) and Dewsnup v. Timm, 112 S.Ct. 773 (1992), Petition, p. 14, he does not contend that the Fifth Circuit's opinion conflicts with either of the cited opinions of this Court. Given the lack of conflict with opinions of this Court and the lack of conflict among the Circuits, this matter does not fit the "special and important reasons" standard of Supreme Court Rule 10.1(c).

2. THE LANGUAGE OF § 506(B) DOES NOT ADDRESS THE ISSUE OF THE RATE OF INTEREST TO BE ALLOWED TO OVERSECURED CREDITORS.

Petitioner correctly contends that the language of § 506(b) and the legislative history are silent as to the rate of interest to be

allowed to oversecured creditors. Petitioner promptly resorts to an analysis of other Code sections which allow interest in order to determine where § 506 fits in a statutory scheme. Petitioner incorrectly contends that because § 502(b)(2) disallows claims for post-petition interest, no reference may thereafter be made to the contract. Petition, p. 19. Nothing in the language of § 502(b)(2) precludes allowance of interest at the contract rate under § 506(b). Allowance of interest to oversecured creditors is an exception to the general prohibition against allowance of post-petition interest.

Petitioner further opines that because the Bankruptcy Code "thoroughly regulates and modifies recovery" of interest in bankruptcy cases, any reference to non-bankruptcy entitlements is precluded. Petition, pp. 25-26. The fallacy in this analysis is apparent from a review of the Code sections dealing with interest. Each of the Code sections which provide for payment of interest in the context of confirmation of a plan of reorganization provide that a creditor shall receive, on account of its claim, payments ". . .of a value, as of the effective date of the plan. . ." of the amount of the creditors claim. See, § 1129(a)(9)(c), § 1129(b)(2)(A)(i)(II),

§ 1129(b)(2)(B)(i), § 1225(a)(5)(B)(ii), and § 1325(a)(5)(B)(ii). Petitioner states that these Code sections require payment of interest at a "market rate." Petition, p.26 Although "market rate" is not the standard stated in the statute, Respondent agrees that the vast majority of courts which have addressed the issue have adopted market rate as the standard.

Petitioner inappropriately cites § 1124(1) and 1322(b)(2) in contending that when Congress intended to leave non-bankruptcy interest entitlements intact, it did so with specific language. First, neither of the cited sections deals specifically with (or even mentions) allowance or rates of interest. Both sections deal with claims which are not modified in any form, including terms and length of repayment, and treatment of security, as well as interest. Second, each of these sections are more appropriately cited for Respondents position. In both instances, Congress has failed to specify a rate of interest other than that which would otherwise apply, and creditors are allowed to retain their non-bankruptcy entitlements. As Congress has demonstrated its ability to clearly abrogate such entitlements when it so intends, its failure to clearly

abrogate non-bankruptcy entitlements to interest in § 506(b) should be considered evidence that it intended that they be retained.

3. THE MAJORITY RULE UNDER THE BANKRUPTCY ACT PROVIDED FOR ALLOWANCE OF INTEREST AT THE CONTRACT RATE AND NOTHING IN THE BANKRUPTCY CODE CHANGES THAT RULE.

Petitioner's second ground for reversal, that historical practice under the Bankruptcy Act does not require application of the contract rate under § 506(b), simply ignores a clear majority rule. Petitioner first contends that because Congress made several changes in treatment of secured creditors regarding which there is no legislative history, the presumption that Congress would always make its intentions clear is rebutted. Petitioner offers as an example claims for attorneys fees under the Act and Code. Petitioner correctly states that under the Act recovery of attorneys fees was generally held to be a matter of state law, and there was no applicable standard of reasonableness. Petition, pp. 36-8. Under § 506(b), however, recovery of attorneys must be provided for in the agreement and must be reasonable. Petitioner trumpets the omission

of any legislative history on this issue as it constitutes a substantial change from pre-Code practice. The lack of legislative history is meaningless in this instance, however, as the change in practice is articulated in the plain language of the statute. Petitioner's example simply fails to prove his point. In fact the converse is true. With respect to attorney's fees, the change in practice is explicit. With respect to interest, the Code simply provides that it be allowed. Since no interest rate is specified, the Court must consider the context in which the statute was enacted.

Petitioner's contention that Act decisions regarding the rate of interest to be allowed are not uniform fails to recognize a clear majority rule that interest be allowed at the contract rate. This rule is evidenced by the cases cited in the Petition. Petition pp. 39-40. Petitioner further notes that several of the contract rate cases decided under the Act were based upon an Act provision which prohibited modification of liens and contends that such analysis is no longer valid because Congress changed the law in enacting the bankruptcy Code to allow modification of liens. Again Petitioner's argument misses the point. When Congress elected to change the law

regarding lien modification, that intention was made clear by specific statutory language. If Congress had also intended to change common practice regarding allowance of interest on oversecured claims, it would no doubt have made its intention equally clear.

Finally, Petitioner contends that this Court should look to § 726(a)(5) as it is the only other Code section dealing with post-petition, preconfirmation interest. Petition, p. 47. The analogy, however, is not analogous. § 726(a)(5) applies only in Chapter 7 cases. § 506(b) applies to cases under any Chapter under the Code. (This case is a Chapter 11, not a Chapter 7.) § 726(a)(5) applies only to solvent estates. § 506(b) applies regardless of whether the estate is solvent or insolvent. § 726(a)(5) applies only to unsecured claims. § 506(b) applies only to oversecured claims. § 726(a)(5) specifies that interest be paid at the "legal rate". § 506(b) does not mention, much less specify, an interest rate. § 726(a)(5) prevents unjust enrichment of the debtor by providing for an additional payment to creditors before any surplus in the estate is returned to the debtor. § 506(b) provides an oversecured creditor with the benefit of its bargain without regard to any benefit

or detriment to the debtor. Clearly, reference to § 726(a)(5) provides no assistance in deciding the rate of interest to be allowed pursuant to § 506(b).

4. THE "EQUITY BALANCING" APPROACH ADVOCATED BY PETITIONER IS AN HISTORICAL ANACHRONISM WHICH NO LONGER HAS ANY APPLICATION.

Petitioner's third ground for reversal, that allowance of interest in bankruptcy is a matter of federal law and deference to state law interest rates is not required, is based upon case law which has been superseded by the enactment of the Bankruptcy Code. Petitioner relies on Vanston Bondholders Protective Committee v. Green, 67 S.Ct. 237 (1946) and its progeny for the proposition that awards of interest are within the discretion of the bankruptcy courts and arise under federal law. That statement may have been true in 1946, but Vanston Bondholders must be considered in its historical context, and that context no longer applies.

Vanston Bondholders was decided under the Bankruptcy Act which was repealed upon enactment of the Bankruptcy Code. The Act, like the Code, contained a general prohibition against

post-petition interest. It did not contain, however, any statutory exceptions like § 506(b) or § 726(a)(5). Because the statutory scheme was considered inequitable, the courts created several equitable exceptions which are administered on a case by case basis. This Court recognized two such exceptions in United States v. Ron Pair Enterprises, Inc., 109 S.Ct. 1026 (1989). The first exception provided interest to creditors if the estate proved solvent. That exception is now codified at § 726(a)(5). The second exception allowed creditors whose claims were secured by income producing securities to apply the income to post-petition interest. That exception no longer exits as such, although it has been incorporated in part in the cash collateral provisions of § 363. A third exception allowing interest to oversecured creditors was deemed to be of "more doubtful provenance." Ron Pair, 109 S.Ct. at 1033. That exception is now codified at § 506(b).

Because there were no statutory exceptions in the Act to the prohibition against post-petition interest, any such exceptions had to be judicially created and awards of interest could only be within the discretion of the courts. In awarding interest, the courts attempted

to "balance the equities" between the various creditors and the debtor. Petition, p. 44. Under the Bankruptcy Code, equity balancing is no longer necessary or appropriate. § 506(b) provides that interest shall be allowed to oversecured creditors. § 726(a)(5) provides that interest shall be allowed to unsecured creditors at the legal rate. The statutory language is mandatory, not discretionary. The courts are not asked or authorized to consider the effect of allowing interest to one creditor on other creditors or the debtor.

Petitioner's analysis also fails to address another key issue. In this case there is an alleged conflict between a federal statute and a state law contract right. As articulated in Ron Pair, however, § 506(b) applies to non-consensual lienholders as well. Petitioner neglects to mention that if this Court adopts its analysis, it will create a real conflict between § 506(b) and 26 U.S.C. § 6621 two federal statutes. [§ 6621 is the statute pursuant to which the interest rate on federal tax liens is calculated.] As this Court will no doubt recall, the creditor in Ron Pair was the Internal Revenue Service, an agency of the federal government.

5. THE FEDERAL JUDGMENT RATE AND § 726(a)(5) HAVE NO RELEVANCE TO RESOLUTION OF THE INTEREST RATE TO BE ALLOWED UNDER § 506(b).

Petitioner's final argument, that the federal judgment rate is logical, practical and equitable, is an incorrect statement of fact and has no legal basis. § 726(a)(5) has no logical relevance to a determination of the interest rate under § 506(b). Section one above contains a detailed comparison which need not be repeated here. It is sufficient to say that there are substantial distinctions in context and application and that any logical nexus between the statutes in minimal. In addition, Petitioner and the Bankruptcy Court contend that the federal judgment rate is logical as the detention of money in a bankruptcy case arises under federal law and is similar to a judgment against estate assets, Laymon, 117 B.R. at 862; Petition, p. 47, and the federal judgment rate is, therefore, an appropriate rate for detaining an oversecured creditor's collateral. Although this simplistic analysis has some visceral appeal, it ignores the more logical comparison to the numerous Bankruptcy Code sections providing for payments to secured creditors in the context of a plan

of reorganization. (After all, Respondent is a secured creditor and this is a reorganization.)

Petitioner's contention that § 726(a)(5) is practical simply ignores the realities of application. What federal judgment rate applies? The rate on the date of filing of the bankruptcy, the date of filing of the motion, the date of the order on the motion, the date of disposition of the collateral, the date of payment of the claim, or does the rate float, changing each time the federal judgment rate changes? Exhibit B to the Bankruptcy Judges order (Petition Appendix, p. A-25) incorporates a floating rate. Since this Chapter 11 was filed September 4, 1984, the federal judgment rate has changed in excess of one hundred times. (The federal judgment rate is based on Treasury bill auctions which occur every four weeks or thirteen times per year.) Changing the interest rate every four weeks for eight years hardly seems "practical" compared to the fixed contract rate.

Finally, Petitioner's argument that the federal judgment rate is "equitable" has no basis in law and is based largely upon factual contentions not supported by the record. Petitioner and the

Bankruptcy Court both appear preoccupied with balancing the equities between the abusive, grasping oversecured creditors and the helpless, downtrodden undersecured creditors, although there is nothing in the record to indicate any impropriety on the part of Respondent. Petition, p. 55; Laymon, 117 B.R. at 863. As recited in Section three above, § 506(b) no longer allows "equity balancing." There is nothing in the language of § 506(b) which would authorize a bankruptcy judge to reduce or deny interest to an oversecured creditor based upon a perceived detriment to any other creditor or the debtor. There is no evidence in the record that allowing interest to Bradford at the contract rate (or any other rate, for that matter) will reduce the distribution to unsecured creditors by so much as one cent.

Petitioner also laments that allowing interest to oversecured creditors at "above market" rates will result in a windfall to those creditors and will encourage them to delay plan confirmation solely to retain those rates. Petition, p. 50. There is nothing in the record to support Petitioner's contention that the contract rate is above market. (Petitioner raises this issue for the first time at this stage of

the appeal.) The contract rate in this case is ten percent per annum, hardly a windfall. Allowing a creditor to receive what it is contractually entitled to is hardly a windfall, either. The only "windfall" in this case is to the debtor who seeks to avoid his contractual obligations. Finally, Petitioner's contention that allowing interest at the contract rate will encourage delay is disingenuous at best. The Petitioner was appointed as the Chapter 11 Trustee in this case on March 6, 1987, over five years ago. The Petitioner has never filed a plan in this case. Any delay in this case has resulted entirely from the Petitioner's failure to conscientiously pursue the duties imposed upon him.

Petitioner's analysis overlooks a great deal of law regarding conflicts between federal bankruptcy law and non-bankruptcy entitlements. In Butner v United States, 99 S.Ct. 914,918 (1979), this Court stated:

> Property interests are created and defined by state law. Unless some federal interest required a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a state serves

> to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving happenstance of bankruptcy. [Citation omitted.]

See also, Wardair Canada, Inc v. Florida Department of Revenue, 106 S.Ct. 2369 (1986). Nothing contained in § 506(b) "requires" that Respondent receive anything other than that to which he is entitled under applicable non-bankruptcy law.

CONCLUSION

Although entitlement to interest in this context is clearly a question of federal law, the rate at which such interest is to be allowed is not addressed by the Bankruptcy Code. the majority rule under the Bankruptcy Act was to allow interest to oversecured creditors at the rate provided in the contract. As there is no indication that Congress intended to change prior practice or to abrogate non-bankruptcy entitlements, Respondent is entitled to

retain his property interests. Respondent requests that this Court deny the Petition for Writ of Certiorari.

Respectfully submitted,

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